



Guidance on Treasury Grant Payments In Lieu Of Tax Credits for Renewable Energy Property

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Presented for New Jersey HMFA

Agenda

- Overview of Section 1603 of the American Recovery and Reinvestment Act (ARRA): Treasury Grant Payments in-lieu of Energy Tax Credits
- Review of Treasury Guidance rules & restrictions
 - Applicant & Project Eligibility
 - Program Timeline Requirements & other information
 - Application Procedures & Required Documentation
 - Use with Lease Structures
 - Recapture
- Tax Accounting
- Questions

Overview

- Treasury guidance released July 9th (<http://www.treas.gov/recovery/1603.shtml>). Treasury began accepting applications July 31st
- Treasury will make payments to qualified applicants in an amount equal to 10% or 30% of the basis of the eligible Property (“Property”), depending on the type of Property
- Property must be placed in service in 2009 or 2010 or must be under construction by 12/31/2010 and completed before the applicable credit determination date
- These payments are not includible in gross income. The basis of the Property is reduced by 50% of the payment amount.
- Property for which a grant payment is received cannot be used to claim either the §48 Investment Tax Credit (ITC) or the §45 Production Tax Credit (PTC)
- Applications will be reviewed and payments made within 60 days from the date the completed application is received by Treasury or placed in service.

Applicant Eligibility

- Ineligible applicants include:
 - Any Federal, state or local government, including any political subdivision, agency or instrumentality thereof
 - Any organization that is described in Section 501(c) of the IRC and is exempt from tax under Section 501(a) of the IRC
 - Clean renewable energy bond lenders, cooperative electrical companies, governmental bodies, OR
 - Any partnership or other pass-thru entity which has any direct or indirect partner (or other holder of an equity or profits interest) which is an organization or entity described above unless this person only owns an indirect interest in the applicant through a taxable C corporation.

Applicant Eligibility

- “Blocker” corporations may be used to avoid this issue.
- Neither a Real Estate Investment Trust (REIT), nor a cooperative organization is a pass-thru entity for this purpose.

Applicant Eligibility

- To be eligible:
 - Applicant must be the owner or lessee of the Property, and
 - Must have originally placed the Property in service.
- Applicants can assign the payment to a third party by submitting a Notice of Assignment along with the application
 - Third party must be a bank, trust company or other financing institution including any federal lending agency
 - Must assign in full and cannot be subject to further assignment
- Foreign persons or entities may be eligible if more than 50% of the person or entity's income is subject to U.S. income tax.
- Eligibility will be determined as of the time the application is received.

Eligible Types of Property

| Specified Energy Property | Credit Termination Date | Applicable Percentage of Eligible Cost Basis |
|-------------------------------|-------------------------|--|
| Large Wind | 1/1/2013 | 30% |
| Closed-Loop Biomass Facility | 1/1/2014 | 30% |
| Open-loop Biomass Facility | 1/1/2014 | 30% |
| Geothermal under IRC sec. 45 | 1/1/2014 | 30% (allowed 10% or 30% but not both) |
| Landfill Gas Facility | 1/1/2014 | 30% |
| Trash Facility | 1/1/2014 | 30% |
| Qualified Hydropower Facility | 1/1/2014 | 30% |
| Marine & Hydrokinetic | 1/1/2014 | 30% |
| Solar | 1/1/2017 | 30% |
| Geothermal under IRC sec. 48 | 1/1/2017 | 10% (allowed 10% or 30% but not both) |
| Fuel Cells | 1/1/2017 | 30% (limited to \$1,500 per 0.5 kW) |
| Microturbines | 1/1/2017 | 10% (limited to \$200 per kW) |
| Combined Heat & Power | 1/1/2017 | 10% |
| Small Wind | 1/1/2017 | 30% |
| Geothermal Heat Pumps | 1/1/2017 | 10% |

Placed In Service

- Qualified Energy Property includes expansions of an existing Property that is qualified Property.
- “Placed in service” means that the Property is ready and available for its specific use.

Placed In Service

- Only for Energy Property placed in service in 2009 or 2010,
OR
- Began construction in either 2009 or 2010,

AND...

Must be completed *prior* to:

- 2013 for wind
- 2014 for certain other Section 45 qualified facilities
- 2017 for Section 48 Property

Beginning of Construction

- Construction begins when “physical work of a significant nature begins.”
- Self Construction – applicant manufactures, constructs, or produces Property for use by the applicant in its trade or business
same rule as above
- Construction by Contract – Property that is manufactured, constructed, or produced on the manufacture, construction, or production of the Property under a written binding contract that is entered into prior to the manufacture, construction or production of the Property
same rule as above

Beginning of Construction

- Safe Harbor
 - Applicant may treat “physical work of a significant nature” as beginning when applicant incurs more than 5% of the total cost of the Property.
 - Costs for planning, designing, securing financing, exploring, or researching the project site are excluded.
 - Economic performance standards of IRC Section 461(h) apply.

Eligible Basis

- The basis of Property is determined in accordance with the general rules for determining the basis of Property for federal income tax purposes.
- Eligible basis includes cost of qualified equipment, installation, labor and derivative soft costs such as permitting, financing and developer fees. Costs of transmission equipment are explicitly excluded.
- Only the cost basis of Property PIS after 2008 is eligible.

Units of Property

- For purposes of determining the beginning of construction of Property or the PIS date, all the components of a larger Property are a single unit of Property if components are functionally interdependent (placing in service of one component is dependent on the placing in service of the other component).
- The owner of multiple units of Property located at the same site and that will be operated as a larger unit may elect to treat the units as a single unit of Property for purposes of determining the beginning of construction and the date the Property is placed in service.



Location of Property

- If the Property is located outside the U.S. during more than 50% of the year, the Property is considered to be used predominantly outside the U.S. during that year.

Original Use

- The original use of the Energy Property must begin with the applicant.
- The cost of used parts cannot be more than 20% of the total cost of the Property.
- If new Energy Property is originally PIS by a person and sold to applicant and leased back to the person by the applicant within three months, unless the lessor and lessee elect, lessor is considered the original user and would be the applicant for the grant.

Application Procedures

- On-line submission process
<https://treas1603.nrel.gov/>
- Applications being reviewed by the National Renewable Energy Laboratory, a division of DOE
- If approved, payments will be made within 60 days from the later of the date of completed application OR the placed in service (PIS) date.

Application Procedures

- For Property PIS in 2009 or 2010, applications must be submitted after the Property is PIS.
- For Property not PIS in 2009 or 2010 but for which construction began in 2009 or 2010, applications may be submitted after construction commences.
- In either case, ALL applications must be received before October 1, 2011.
- If an applicant is applying for payments for multiple units of Property on the same site that are treated as a single, larger unit of Property, all such units may be included in a single application.

Application Procedures

- A completed application includes the signed and completed application form, supporting documentation (detailed cost breakdown), signed Terms & Conditions and completed payment information
- For applications requesting a grant payment greater than \$1 million, supporting documentation includes an independent accountant's certification (takes the form of an Examination Report)
- For applications requesting a grant payment greater than \$500,000 but less than \$1 million, supporting documentation includes an independent accountant's Agreed-Upon Procedures Report

Application Procedures

- If application is approved, a notice will be sent to applicant.
- Treasury is expected to make payment no later than 5 days from the notice date.
- Payment will be made via Electronic Funds Transfer.
- A final cost “true up” is not permitted after the grant is paid.

Application Procedures

- If applicant has not submitted sufficient information, applicant will be notified and has 21 days from the notice date to submit additional information.
- If additional information is not received within the 21 day period, application will be denied.



Application Procedures

- If determined that the application does not qualify for payment, the applicant will be notified.
- Notification will include the reasons for the determination and will be considered the final agency action on the application.

Required Documentation

- **Eligible Property**
 - Design plans
 - Final engineering design documents stamped by a licensed professional engineer
 - Documents establishing nameplate capacity

- **Placed In Service**
 - Commissioning report
 - Interconnection agreement (only for properties interconnected with a utility)

Required Documentation

- Under Construction (not PIS)
 - Paid invoices for work actually performed
 - Other financial documents demonstrating that “physical work of a significant nature” has begun
 - Binding contract (meeting the requirements of the guidance)

- Leased Property
 - Written agreement between the lessor and lessee meeting the requirements of the guidance

- Independent Accountant’s certification required if over grant payment is over \$500,000

Leased Property

- A lessor may irrevocably elect to pass-through the payment to a lessee.
- The lessor and lessee must agree in writing, that the lessor waives all right to a Section 1603 payment or a PTC or ITC with respect to the Property, BEFORE the lessee may apply for a Section 1603 payment with respect to such Property.

Leased Property

- The lessee must agree to include 50% of the payment ratably in gross income over the five year recapture period.
- Both the lessor and the lessee must be persons eligible to receive a payment.
- This election may not be made by a lessor that is a mutual savings bank or similar financial organization, a regulated investment company or a real estate investment trust.

Sale Leaseback Transactions

- The lessee may claim the payment if:
 - The lessee originally placed the Property in service.
 - The Property is sold and leased back by the lessee, within three months after the date the Property was originally placed in service.
 - Neither the lessee nor the lessor make an election to preclude application of the sale-leaseback rules.

Recapture

- If the applicant disposes of the Property to a disqualified person or the Property ceases to qualify as a specified energy Property within 5 years from the PIS date, a certain percentage of the payment must be repaid to Treasury.
- Property is considered disposed if any interest in the Property is sold to a disqualified person.
- Temporary cessation will not result in recapture if the owner “intends to resume production.”

Recapture

- Property ceases to qualify if the use of the Property changes so that it no longer qualifies as specified energy Property.
- Permanent cessation will result in recapture (unless if permanent cessation is due to natural disaster).

Recapture

- If a lessor elects to pass through the payment to a lessee and the lessor sells the Property to a disqualified person, the lessee is liable to the Treasury for the recapture amount.
- If the lease is terminated and possession of the Property is transferred to the lessor or any other person, the lessee is liable to the Treasury for the recapture amount if the use of the Property changes during the recapture period so that it no longer qualifies as specified energy Property.

Tax Accounting

- The legislation refers to this as a grant but the statute states that it's not includible in gross income.
 - This is not "tax exempt income"
 - Guidance still lacking but should be a "tax exempt receipt"
- The grant is cash but we don't yet have guidance on what impact that cash will have on the tax return balance sheet (debit/credit).
 - This should be an increase to equity because the grant is a substitute for tax equity
- Statute says you make a basis reduction equal to 50% of the grant amount.
 - Guidance lacking, but it should follow that partner's capital accounts should be increased for the 1603 payment amount, then reduced for this adjustment

Tax Accounting

- Payments passed to Lessee
 - Section 1603 and guidance are unclear, but...
 - Lessee should report income ratably over 5 years.
 - Capital account of lessee partners should increase.
 - Should not be reduction to lessor's basis

- Payments Assigned to third party financial institution
 - Again, no guidance...
 - Will the Applicant (owner) make the 50% basis adjustment or will the Assignee recognize income equal to 50% of the assigned payment ratably over 5 years?

Tax Accounting

- Solar and most other renewable energy property is 5-year personal property
 - Bonus depreciation (50%) for renewable energy property placed in service in 2009
 - Several depreciation options available. Example below assumes a \$500K energy project that received a \$150K Treasury grant, thus has \$425K in depreciable basis (after 50% basis reduction):

| | 5-Year MACRS with Bonus | | 5-Year SL with Bonus | | 12 Year ADS |
|---------|------------------------------------|---------------------|---------------------------------|---------------------|--------------------|
| | 5-Year MACRS | Depreciation | 5-Year SL | Depreciation | |
| Year 1 | (85,000) | (255,000) | (42,500) | (233,750) | (17,708) |
| Year 2 | (136,000) | (68,000) | (85,000) | (42,500) | (35,417) |
| Year 3 | (81,600) | (40,800) | (85,000) | (42,500) | (35,417) |
| Year 4 | (48,960) | (24,480) | (85,000) | (42,500) | (35,417) |
| Year 5 | (48,960) | (24,480) | (85,000) | (42,500) | (35,417) |
| Year 6 | (24,480) | (12,240) | (42,500) | (21,250) | (35,417) |
| Year 7 | - | - | - | - | (35,417) |
| Year 8 | - | - | - | - | (35,417) |
| Year 9 | - | - | - | - | (35,417) |
| Year 10 | - | - | - | - | (35,417) |
| Year 11 | - | - | - | - | (35,417) |
| Year 12 | - | - | - | - | (53,125) |

Twining with LIHTC, HTC & NMTC

- You can potentially claim the LIHTC on renewable energy property
 - Guidance is still lacking on whether you can claim the LIHTC on property you received the Section 1603 grant for. However, you can claim the LIHTC with the ITC...
 - Cannot sell electricity
 - Is renewable energy property commercial property?
 - Amount that gets into LIHTC basis is the net basis in the renewable energy property after the reduction for 50% of the ITC.
- You CANNOT claim the Historic Tax Credit (HTC) on renewable energy property.
- New Markets Tax Credits (NMTC) structures can work well leveraging ITC equity and potentially could work leveraging the grant payment via the ability to assign it or distribute it to a partner.



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